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New Tangible Property Regulations; Simplified Option Available to Many Small Businesses

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Federal law allows taxpayers to deduct all the ordinary and necessary expenses they incur during the taxable year in carrying on their trade or business, including the costs of certain materials, supplies, repairs, and maintenance. However, taxpayers are required to capitalize the costs of acquiring, producing, and improving tangible property, regardless of the size or the cost incurred.

In 2013, the Internal Revenue Service issued [final regulations](#) clarifying how federal tax law applies to tangible property. In general, the new rules apply to taxable years beginning on or after Jan. 1, 2014. For most taxpayers, this means the returns they file during 2015 and later years. Earlier this year, the IRS also developed a special [simplified](#) procedure available to many small businesses.

Section 162 of the Internal Revenue Code allows taxpayers to deduct the ordinary and necessary expenses of carrying on their trade or business, including the costs of certain materials, supplies, repairs and maintenance.

However, section 263(a) of the Code requires taxpayers to capitalize the costs of acquiring, producing and improving tangible property, regardless of the size or the cost incurred.

Capitalized costs generally are recovered through depreciation for tangible property or amortization for intangible property. To ease the administrative burden faced by small business taxpayers that want to apply the tangible property regulations, and do not wish to compute a section 481(a) adjustment, the IRS has provided a simplified procedure that can be used for the first taxable year beginning in 2014.

Under this procedure, an eligible small business may choose to change to certain methods of accounting under the regulations by taking into account only amounts paid or incurred in taxable years beginning on or after Jan. 1, 2014. Small businesses that make this choice will not have a section 481(a) adjustment for the first taxable year beginning in 2014, and will not be required to file [Form 3115](#), Application for Change in Accounting Method. This procedure permits a small business to implement the final regulations on a prospective basis.

It also outlines common tax areas that affect small business taxpayers and information needed for filing returns for 2014 and subsequent tax years.

A set of [questions and answers](#) , posted on IRS.gov, can help interested taxpayers and tax preparers better understand the tangible property regulations and the simplified option for small business. Further details on the simplified option can also be found in [Revenue Procedure 2015-20](#).